Office-Supreme Court, U.S.
FILED
SEP 27 1963
JOHN F. DAVIS, CLERK

In The

# SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1963

3354

On Petition for Writ of Certiorari to the Court of Appeals for the Fourth Circuit

## BRIEF FOR RESPONDENT IN OPPOSITION AND APPENDIX

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**In The**

**SUPREME COURT OF THE UNITED STATES**

OCTOBER TERM, 1963

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No. .....

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NORTH CAROLINA NATIONAL BANK,
*Petitioner,*

vs.

UNITED STATES CASUALTY COMPANY,
*Respondent.*

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**On Petition for Writ of Certiorari to the Court of Appeals for the Fourth Circuit**

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# BRIEF FOR RESPONDENT IN OPPOSITION

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## OPINIONS BELOW

This action was tried in the District Court for the Western District of North Carolina to the Court without

a jury, following which judgment was rendered in favor of the defendant based upon the findings and opinion reported at 208 F. Supp. 452. On appeal to the United States Court of Appeals for the Fourth Circuit, the judgment of the District Court was affirmed in an opinion reported at 317 F. 2d 304, which is printed as an appendix to the Petition herein.

## QUESTION PRESENTED

Petitioner's statement of the question presented for review assumes that an ambiguity exists in the wording of the bond sufficient to afford an indemnity thereunder, whereas the terms of the bond are not ambiguous, as held by the Court of Appeals in this and its earlier decision, and as held by six other appellate courts.

The question presented by this case is whether or not plaintiff's losses from the failure of its borrower to repay loans of money are covered by Clause (E) of the bond (reprinted as appendix hereto) which insured plaintiff against any loss resulting from its having extended credit "on the faith of . . . securities, documents or other written instruments which prove to have been counterfeited or forged as to the signature of any maker, drawer, issuer . . . or as to the signature of any person signing in any other capacity . . ."

## STATEMENT OF THE CASE

In this action, the plaintiff, petitioner, sought to recover upon an indemnity bond issued by the defendant to a predecessor corporation of the plaintiff, losses sustained by reason of the failure of C. K. Callahan and Sons Lum-

ber Company to repay loans made to the Lumber Company over a period of about nine years. To secure the payment of such loans, the Lumber Company had assigned accounts receivable, two-thirds of which were non-existent.

In its complaint, petitioner alleged that its losses resulted from the making of loans in reliance upon duplicate invoices representing accounts receivable which "proved to have been *counterfeited*" (Complaint paragraphs 9, 11, and 12, pages 5 and 6 of appendix to plaintiff's brief in the Circuit Court), and that its losses were therefore covered by Clause (E) of the bond.

In its complaint and in the trial court, petitioner did not contend that the duplicate invoices involved were "forged as to the signature".

The trial Court rendered its decision in favor of the defendant based upon the recent decision of the Fourth Circuit Court of Appeals in the case of *First National Bank of South Carolina* vs. *Glens Falls Insurance Company*, 4th Cir., 304 F. 2d 806, in which the Court held that similar fictitious invoices were not "counterfeited or forged as to the signature" of any person and were not within the coverage of Clause (E) of an identical bond.

Thereafter, in its brief on appeal to the Court of Appeals, the petitioner advanced for the first time the argument that under the law of North Carolina the plaintiff's losses are covered by the words "forged as to the signature" appearing in Clause (E) of the bond sued upon.

The Court of Appeals affirmed the judgment of trial court in an opinion in which another panel of Circuit Court Judges adhered to its earlier decision in the First National

Bank of South Carolina case, and discussed and rejected all arguments advanced by petitioner.

The facts herein involved are very aptly summarized and stated throughout the opinion of the Court of Appeals, set forth as an appendix to the petition. For emphasis and an additional statement, we call attention to the following facts:

The plaintiff seeks to recover only upon the provisions of Insuring Clause (E) of the bond reading in part as follows:

> "(E) SECURITIES—Covering:—Any loss through the insured's having in good faith and in the course of business . . . given any value or extended credit . . . on the faith of . . . any securities, documents, or other written instruments which prove to have been counterfeited or forged as to the signature of any maker, drawer, issuer, or as to the signature of any person signing in any other capacity . . .".

The full text of Clause (E) of the bond is reprinted as an appendix hereto.

In addition, the bond provided under "EXCLUSIONS—Section 1", the following:

> "THIS BOND DOES NOT COVER:
>
> "(d) Any loss the result of the complete or partial non-payment of or default upon any loan made by or obtained from the insured, whether procured in good faith or through trick, artifice, fraud or false pretenses, except when covered by Insuring Clauses (A), (D), or (E)".

In the years before 1950, petitioner made loans to the C. K. Callaham and Sons Lumber Company, of Charlotte, N. C., hereinafter referred to as the "Lumber Company", secured by the assignment of various accounts receivable owed the Lumber Company. The loans were evidenced by various promissory notes in which the Lumber Company assigned to the bank several specified and described accounts receivable. In these early years, the customers of the Lumber Company whose accounts were assigned were notified of the assignment of the account and were requested to remit payment thereof direct to the bank. Such a notification appeared in a typed notice on the original invoice which was sent to the customer of the Lumber Company, which notice read:

> "For value received, this account has been assigned to the American Commercial Bank, Charlotte, N. C. to whom please remit.
>
> C. K. Callaham and Sons Lumber Company
>
> By. .....
>
> President"

Sometime before 1950, the practice of notifying customers of the Lumber Company of the assignments was discontinued, and the accounts assigned were thereafter paid to the Lumber Company, which deposited payments in its own checking account at the plaintiff bank. Duplicate copies of invoices for these accounts were delivered to the Bank. As pointed out by the Court of Appeals, "the Bank regularly reviewed Callaham's financial statements and its customer ledger accounts, and by such means acquired assurance that Callaham did have a substantial volume of business, a substantial volume of outstanding receivables

and that the invoices, copies of which were deposited with it, represented actual outstanding receivables."

Sometime in 1950, after J. W. Callaham succeeded his father as President and in the active management of the Lumber Company, business began to decline, and J. W. Callaham began assigning to the bank non-existent accounts receivable which he had fabricated. As testified to by J. W. Callaham, he would prepare or have his secretary type up invoice or purchase orders on his company forms, destroy the original or ribbon copy of the invoices, and attach a duplicate copy of the invoice to a new collateral note specifying the assignment of such accounts to secure payment of the note. These fictitious accounts receivable were entered upon a ledger page of the ledger book of the Lumber Company in every detail similar to its genuine accounts receivable, and were reflected in its record of sales and in the financial statements given the bank each year. The second carbon copy of the invoice was placed in the customer's folder in the Lumber Company office.

Notwithstanding the discontinuance of the practice of notifying the customers of the Lumber Company that the accounts had been assigned to the Bank, the Lumber Company continued to place on the duplicate copies of the invoices the above notation. On 100 of the duplicate invoices herein involved, this notation appeared and was signed by J. W. Callaham as President and Treasurer of the Lumber Company. (Appellant's appendix page 10). On the other 14 duplicate invoices herein involved, there was an unsigned notation that the account had been assigned to the Bank to secure a loan. The purpose served by these notations, which did not appear on the original invoices after 1950, was not explained.

The books and records of the Lumber Company were inspected at periodic and irregular intervals of time by the officers and representatives of the plaintiff bank for the purpose, as they testified, of determining that the assigned accounts were genuine and outstanding as represented by J. W. Callaham. These officers testified that they relied upon the ledger accounts, the oral statements and representations of Callaham and his bookkeeper, the sales records, and the yearly financial statements, as indications that the assigned accounts receivable were genuine.

The means by which Callaham practiced his fraud and by which the Bank was misled was shown by the testimony of the witness Cooper, Senior Vice-President of plaintiff bank set forth on pages 59-66 of the appendix to defendant's brief filed with the Court of Appeals. There Mr. Cooper testified that statements prepared by officer's of borrower's "are accepted for credits"; that the bank officials carefully examined and analyzed the financial statements furnished the bank by Callaham to determine the financial condition of the Lumber Company, and that these statements showed the existence of large amounts of genuine accounts receivable. He stated that the Bank made inquiries concerning the credit standing of the customers whose accounts had been assigned *"in order to satisfy ourselves that we were accepting invoices of companies in existence* and companies that had credit ratings with their banks". (appx. p. 60) He further stated that the Bank required its borrower to keep records showing the sales it made, that Callaham kept such records in the form of general sales records and a ledger account or page for every account receivable assigned to the bank, and that each such ledger page, for both genuine and fictitious accounts contained a record of sales, deliveries, and other

entries, "showing activity, credits and debits". Mr. Cooper also testified that Callaham's bookkeeper told him the assigned accounts were genuine when he periodically gave him an "aging" of the accounts assigned, but that he still checked his records *"to see that we had genuine accounts, to see that they were accounts receivable"* (ibid. appdx. p. 63).

Finally, Mr. Cooper testified:

"A. The loans were based on the company's own representation of its financial condition.

Q. And the representation that the accounts receivable were genuine and actually in existence?

A. Yes, as borne out by their records, by their ledger records.

Q. And as borne out the representation of J. W. Callaham himself?

A. Yes." (ibid. appdx. p. 63).

To complete the masquerade, Callaham, upon the occasions of Mr. Cooper's personal visits to his office, would be found busily engaged in taking or pretending to take telephone orders, giving Mr. Cooper the impression that he was going great guns with the business.

On July 1, 1959, as the result of some new procedure established by the bank, all of the promissory notes of the Lumber Company were consolidated into one collateral note of $300,000, secured by the assignment of the various accounts receivable *specified in a list attached thereto*, which were assigned to the bank in accordance with the terms of a collateral loan agreement executed by the Lumber

Company. In part, this agreement provided that by the assignment of each account receivable, the Lumber Company represented to the bank that each account was genuine and outstanding in the amount shown and specified for each account, that there were no set-offs or chargebacks, and that no other amount should be credited to the account. These were the same representations which J. W. Callaham had made with respect to each account receivable it had previously assigned to the bank.

The assignment of the specified accounts receivable was completed when this note and loan agreement was executed, with the list of accounts attached thereto. Callaham continued to deposit with the Bank copies of invoices representing, or which he stated represented, the accounts assigned, on which appeared the "notification" of assignment which had previously been placed on the original invoices sent to the customers.

On August 14, 1959, an official of one of the firms the account of which had been assigned to the plaintiff, who happened to be in the bank, was asked about his account with the Lumber Company which appeared to be past due. Upon this inquiry, the Bank discovered that no such account was due the Lumber Company, which led to further inquiry of J. W. Callaham and the discovery of the fact that three-fourths of the accounts pledged to the Bank by the Lumber Company were fictitious. The total amount of all accounts receivable assigned the Bank at that time was $414,017.10, and the total indebtedness of the Lumber Company to the Bank was $291,397.39. After crediting collections of valid accounts receivable and dividends from the trustee in bankruptcy of the Lumber Company, a total

loss of the Bank was reduced to $211,474.70, which is the final amount claimed by plaintiff in this action.

## SUMMARY OF REASONS WHY WRIT OF CERTIORARI SHOULD NOT BE GRANTED

1. This Court has recently declined to review the question here presented in *First National Bank of Memphis* vs. *Aetna Casualty and Surety Company*, 6 Cir. 306 F. 2d 702, certiorari denied, March 25, 1963, 372 U. S. 953, 9 L. Ed. 2d 977, 83 S. Ct. 951.

2. No embarrassing conflict exists between the decisions of the United States Courts of Appeal upon the question here presented which requires resolving by a decision of this Court.

3. The decision of the Third Circuit upon which petitioner relies, *Fidelity Trust Company* vs. *American Surety Company of New York*, 288 F. 2d 805 (1961), was against the weight of authority when rendered, namely, *Torrance National Bank* vs. *Aetna Casualty & Surety Company*, 6 Cir., 252 F. 2d 699; *Pasadena Investment Company* vs. *Peerless Casualty Company*, 132 Cal. App. 2d 328, 282 P. 2d 124; *Fitzsimmons Boiler Company* vs. *Employers Liability Assurance Corp.*, 2 Cir., 105 F. 2d 893. The decision in the Fidelity Trust Company case has been subsequently rejected by the Sixth and Eighth Circuit Courts of Appeal, by the Fourth Circuit in 1962 and in the instant case and by the Supreme Court of Colorado. *First National Bank of Memphis* vs. *Aetna Casualty & Surety Company*, 6 Cir., 306 F. 2d 702; *State Bank of Fond du Lac* vs. *Maryland Casualty Company*, 8 Cir., 288 F. 2d 44; *United States Fidelity & Guaranty Company* vs. *First National Bank*

*of Fort Mountain*, (1961) 147 Cal. App. 2d 440, 304 P. 2d 202. *First National Bank of South Carolina vs. Greenville Falls Ins. Company*, 4th Cir. 1962, 304 F. 2d 880, Opinion of Court of Appeals herein, printed as Appendix to petition.

4. Petitioner's contention as to "forged as to the signature of" involved the correctness of the Court of Appeal's interpretation of North Carolina law which should not be reviewed by this Court. The decision of the Seventh Circuit upon which petitioner relies, *Second National Bank of Durand vs. Fidelity and Casualty Company*, 246 F. 2d 582 (1957), was based upon a prior local decision which represents a minority view of the law of forgery. Such is not in accord with the law of North Carolina relating to forgery. The reasoning of this decision was rejected by the Third Circuit in the Fidelity Trust Company case, *supra*, and by all of the other Courts which have considered the question involved.

5. The additional facts appearing in the instant case and the clarity and cogency of the opinion of the Court of Appeals herein resolve any doubt as to the question presented.

6. This action involves a private dispute between private parties, the provisions of which are subject to change by the parties, and petitioner's claim as a National Bank which was acquired after the discovery of the losses by plaintiff's predecessor is not relevant.

7. The rule of construction by which the rights of the parties to this North Carolina contract are to be determined is well settled by the decisions of the North Carolina Supreme Court and of this Court.

In its complaint the plaintiff, petitioner, based its cause of action upon the sole contention that the duplicate invoices were "counterfeited", and plaintiff in the trial court based its case entirely upon the decision in Fidelity Trust Co. v. American Surety Company, *supra*. In its brief to the Court of Appeals petitioner, for the first time, also contended it had coverage "In view of the bond which reads: —Forged as to the signature". Both contentions are advanced by petitioner in its petition to this Court.

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For the convenience of the Court, and at the risk of repeating the reasoning of the Court of Appeals, which we would not presume to attempt to improve upon, and the arguments set forth in our brief in the Court of Appeals, we have collated and discussed hereinafter the authorities and facts supporting our reasons why the petition should not be granted.

## ARGUMENT AMPLIFYING REASONS WHY A WRIT OF CERTIORARI SHOULD NOT BE GRANTED

*This Court has recently declined to review the same question here presented.*

This Court on March 25, 1968, declined to review the same question herein involved in *The First National Bank of Memphis vs. The Aetna Casualty and Surety Company, supra*.

In the Bank of Memphis case, the Sixth Circuit Court of Appeals held that warehouse receipts which were signed by the warehouseman purporting to represent Soya beans which did not in fact exist in the warehouse were covered

by the terms of Clause (E) of the identical bond herein sued upon, stating in its opinion with reference to this point as follows:

> "In our opinion, the warehouse receipts were not forged or counterfeited. They were signed and issued by the elevator company and endorsed by Butler-Foster, all by duly authorized officers. Falsity lies in the representation of facts contained in the warehouse certificates and not in the genuineness of their execution. In common parlance, the warehouse certificates would not be considered as forged or counterfeited and certainly not at common law or under the statutes of Alabama or Tennessee."

In its opinion in that case, the Sixth Circuit Court of Appeals cited with approval the many decisions hereinafter discussed supporting its interpretation of the Bankers Blanket Bond involved, and pointed out that the decisions relied on by petitioner herein stand alone and rejected by all other courts which have considered the question, including the Fourth Circuit in *First National Bank of South Carolina* v. *Glens Falls Ins. Co.*, *supra*.

Thereafter, the Fourth Circuit Court of Appeals rendered its opinion in the instant case in an opinion, the clarity and cogency of which should remove any vestige of uncertainty as to the law upon the question here involved.

In its petition to this Court for a Writ of Certiorari, the First National Bank of Memphis stated:

> "There is a conflict between this decision of the Court of Appeals for the Sixth Circuit and the earlier decision of the Court of Appeals for the Third

Circuit. This conflict is regarding a matter of great importance to all National Banks, Federal Savings and Loan Associations, as well as other banking institutions insured by Bankers Blanket Bonds or similarly worded bonds."

The same contentions are advanced with less validity in the petition in the instant case. The warehouse receipts involved in the Bank of Memphis case constituted documents which purported to be of legal significance and intrinsic value because they obligated the signing warehouseman to produce upon their presentment the Soya beans they represented. The papers herein involved called duplicate invoices were nothing more than purported carbon copies of bills or statements of account of the Lumber Company to its customer, unaccepted and unacknowledged by the customer, which obligated no person and possessed no legal or intrinsic value, and which was not even accepted by the plaintiff Bank as proof of the existence of the accounts indicated thereon.

Therefore, for even stronger reasons than existed in the Bank of Memphis case the petition herein should also be denied.

*Clause (E) of the bond covers only documents which are counterfeited as to signature of a maker or person signing in any other capacity, which does not include the duplicate invoices in question.*

The terms of Clause (E) of the bond upon which plaintiff relies are not ambiguous. The petitioner has heretofore argued that these provisions are plain and entitled it to recover because the [illegible] counterfeited

should not be held to be modified by the phrase "as to the signature of" in the first sentence of Clause (E).

The Court of Appeals in its opinion herein answered and laid to rest for all time this contention in the following language:

> "In First National Bank of South Carolina v. Glens Falls Ins. Co., 304 F. 2d 806, we held that invoices which were fictitious because of falsity of their implicit representation that a corresponding, collectible account receivable existed were not 'counterfeited or forged as to the signature of anyone.' In dealing with the contention there that the word 'counterfeited' was not qualified by the words 'as to the signature,' we said:
>
> > "'In our judgment the limitation cannot be ignored. It is familiar law in South Carolina and elsewhere that the terms of an insurance contract must be construed in favor of the insured and against the insurer where the words of the policy are ambiguous, but where there is no ambiguity a contract of insurance like other contracts, must be construed according to the plain and ordinary meaning of its terms. Pitts v. Glens Falls Indemnity Co., 222 S.C. 133, 72 S.E. 2d 174; Quinn v. State Farm Mut. Automobile Insurance Co., 258 S.C. 301, 120 S.E. 2d 15. The meaning of the contract on the face of it that seems to us to be plain. Protection is afforded to the insured against loss incurred by extending credit on a written instrument that is found to have been counterfeited or forged as to the signature. There is no comma after the word 'counterfeited' and no other indication that the clause was not

qualify both terms of evil import; and there is positive indication that it is the counterfeited or forged signature to the fraudulent document rather than false statements in the document or the falsity of the document in its entirety which alone gives rise to the liability of the insurer. Thus, there is reference in the bond after the words 'counterfeited or forged' to the signature of any maker, drawer, issuer, endorser, assignor, lessee, transfer agent or registrar, acceptor, surety or guarantor, or as to the signature of any person signing in any other capacity. Obviously, counterfeited as well as forged written instruments may be signed and we do not think that it can fairly be said that this list of persons refers only to forgeries and not to counterfeits. Also included in the section is a clause as to loss incurred by relying on written documents which prove to have been 'raised or otherwise altered or lost or stolen.' As to these no mention of the signature is made, thus creating a special class of documents which may give rise to liability whether the signature is genuine or not. The omission of the phrase, as to the signature, in describing this class of documents and the inclusion of the phrase in the description of the documents first mentioned above is worthy of note. Immediately following it the clause having guaranteed or witnessed a signature, again demonstrating the emphasis placed by the draftsman on the signature rather than on the contents of the writing, or its falsity as a whole. At the end of Section (E) of the bond it is provided that mechanically reproduced facsimile signatures are treated the same as handwritten signatures and no reason appears why this more liberal provision

> should be applied to forged but not to counterfeited instruments. Finally, there is the significant exclusion clause that losses which result from the non-payment of a loan obtained by fraud or false pretenses are not covered by the bond. This provision obviously shows that the bond is not intended to cover losses incurred through reliance on false pretenses generally unless the fraud is accomplished by the use of a counterfeited or forged signature.'"

In its opinion the Court of Appeals further concluded as follows:

> "The papers by which such misrepresentation were effectuated, having no intrinsic value in themselves and being non-negotiable, are not the usual subject of counterfeiting or forgery. When they are fictitious only in the sense that they contain an implicit or explicit representation that a valid, collectible, but uncollected, receivable exists, it is very doubtful, whatever writing appeared upon them, they could be held to be the subject of counterfeiting or forgery so long as the writing did not misrepresent their origin".

This decision is in accord with the many other decisions upon the same or similar questions cited in our previous brief and discussed for convenience below.

In *State Bank of Poplar Bluff vs. Maryland Casualty Company, supra*, the plaintiff sued upon the same bond here involved to recover losses it suffered from the non-payment of loans secured by chattel mortgages on automobiles which were not in existence or in the possession

of the mortgagor. The court held that the mortgages were neither counterfeited nor forged within the meaning of the bond.

This case also involved documents which in genuine have legal significance and value, whereas duplicate invoices have no intrinsic value.

The decision of the Eighth Circuit in that case has been accepted by the State Courts as well as other Circuits as stating the correct interpretation of the bond.

In the case of *United States Fidelity and Guaranty Company* vs. *First National Bank of Fort Morgan*, *supra*, the Colorado Supreme Court, with reference to the Bank of Poplar Bluff decision, said:

"The rule announced therein is unquestionably supported by the great weight of authority."

In that case, the Colorado Supreme Court considered the identical bond and fact situation here involved. In holding that the bond did not cover losses resulting from the non-payment of loans secured by the assignment of fictitious accounts receivable represented by fabricated invoices, the Colorado Court said:

"It is clear from the language of the bond that the liability of the guaranty company is limited to instruments which have been counterfeited or forged as to the signature of any maker, drawer, etc. It is not contended here that a false signature appeared upon any of the invoices involved. The words com-

terfeited or forged even though not specifically connected to the signature upon an instrument, do not include in their meaning the making of a false statement of fact within the body of an instrument otherwise genuine."

As before stated, the decision in *Fidelity Trust Company* vs. *American Surety Company*, *supra*, was a complete departure from the weight of authority at that time as represented by the following decisions:

*Pasadena Investment Co.* v. *Peerless Casualty Co.*, *supra*; involving a claim for losses resulting from the non payment of loans secured by the assignment of accounts receivable which did not exist and the use of fictitious duplicate invoices as in the instant case. The bond involved in that case was the Bankers Blanket Bond covering losses resulting from loans made upon "securities, obligations or other written instruments which prove to have been forged, counterfeited, raised or otherwise altered." The California Court held that the duplicate invoices involved were neither counterfeited nor forged.

The Bankers Blanket Bond there involved was in the form of the bond before it was revised by adding to the words "counterfeited" and "forged" in Clause (E) the words "as to the signature of".

*Torrance National Bank* vs. *Aetna Casualty and Surety Company*, *supra*, in which it was held that a check of a corporation signed by its treasurer with an authorized but did not constitute a forgery under the bond herein involved.

*Fitzsimmons Bolder Co., Inc.* vs. *Employers Liability Assurance Corp. Ltd.*, *supra*, in which the Second Circuit

Court of Appeals held that checks signed by officers of a corporation who were induced to sign by fraudulent representations of the treasurer by means of fictitious vouchers, did not constitute forgery within the bond sued upon.

In *Fidelity Trust Company* vs. *American Surety Company*, *supra*, relied upon by petitioner, and which now stands alone and rejected, the Court ignored the phrase "as to the signature of" in Clause (E), as well as the factual and legal insignificance of a duplicate invoice, which the opinion and the facts appearing in the instant case so graphically demonstrated. Apparently, the Court of Appeals in that case was greatly influenced by its previous decision in *Provident Trust Company* v. *National Surety Co.*, 3rd Cir. (1943), 138 F. 2d 252. In the latter case, it was held that warehouse receipts for goods that did not exist were covered by the Bankers Blanket Bond covering instruments were "forged or altered" under Clause (D) of the bond. Since that decision the wording of Clause (D) of the Bankers Blanket Bond was revised to cover only "instructions or advices which *bear the forged signature*" of a person. Under the statutes of Pennsylvania, the Court of Appeals held that the fictitious warehouse receipts constituted forgery. These statutes were different from those of North Carolina or Missouri.

As pointed out above, the Sixth Circuit Court of Appeals in the Bank of Memphis case held that properly signed warehouse receipts for beans that were not in the warehouse did not constitute forged documents within the meaning of either Clause (D) or Clause (E) of a similar bond.

In its opinion the Court of Appeals further pointed out that the presentation of the duplicate invoices was merely

another form of falsely representing that the accounts assigned were genuine and a form of deceit specifically excluded from the bond, saying:

> "These same representations were contained in more explicit form in the loan agreement, though the Bank, and apparently no one else, has suggested that the loan agreement, on that account, is counterfeited or forged as to signature. The financial statements which the Lumber Company filed with the Bank and upon which the Bank relied were equally false, for they included in reported accounts receivable all of these spurious transactions. The ledger sheets which reflected these fictitious transactions which the Bank inspected and upon which the Bank relied were similarly false, but no more can be said of any of these instruments, including the duplicate invoices, than that they were all part of the scheme of misrepresentation of the Lumber Company's sales and outstanding receivables. All of them were clearly the acts of Callahan and the Lumber Company, and there was no misrepresentation of the person or persons responsible for them."

Had it been necessary, the Court of Appeals might well have concluded that invoices were not the documents or instruments covered by Clause (E) as did the Massachusetts Court in *Rockland Athys. National Bank v. Massachusetts Bond and Indemnity Co.*, (Mass. 1950), 157 N.E. 2d 235. In that case it was held that a letter purporting to certify the correctness of a borrower's financial statement upon which the signature of a Certified Public Accountant had been forged, was not within the coverage of Clause (E) of the bond herein involved. A similar

conclusion was reached by the English Court in *Equitable Trust Company v. Henderson*, (1930) 47 Times L. 90, in which a false financial statement was held not to be the subject of forgery.

The other decisions on the question here presented were made upon fact statements alleged or stipulated. Here, the facts were developed by the testimony of the participants, C. K. Callaham and officials of the plaintiff bank. This testimony showed beyond any question the true nature of accounts receivable financing, the insignificance of the duplicate invoices, the fact that the Bank made its own investigation of the records of its borrower, and in reality made its loans in reliance upon these records and its conclusion that the Lumber Company had a prosperous business.

*The duplicate invoices were neither "forged" nor "altered as to the signature of any person" under the law of North Carolina.*

In its complaint and throughout the trial of this case, petitioner did not contend or argue that the duplicate invoices were "forged as to the signature of" any person, apparently rejecting such argument as untenable. Petitioner's counsel made such an argument for the first time in his brief to the Court of Appeals.

Petitioner's argument on this point is based upon the decision of the Seventh Circuit in *Security National Bank of Poland v. Fidelity and Casualty Company of New York*, 24 F. 2d 582 (1957), and the North Carolina decision in *Peoples Bank and Trust Company v. Fidelity and Casualty Company*, 238 N.C. 510, 77 S.E. 2d 800

Neither of these decisions has any application to the facts of the instant case.

The decision in the Bank of Durand case was based squarely upon the decision of that Court of Appeals in *Quick Service Box Company* v. *St. Paul Mercury Indemnity Company*, 7th Cir., 95 F. 2d 15, interpreting the statutes of the state concerning forgery, and holding that the filling in by an office manager of blank checks signed by officers of his company and covering the same to the office manager's use constituted forgery. The Court pointed out in its opinion however that "Quick apparently represents a minority view", a view contrary to the decisions of many other courts, particularly *Fitzgibbons, Boiler Company* v. *Employers' Liability Assurance Corporation, supra*, and other decisions cited in 37 C. J. S. Forgery, Sec. 8.

The Seventh Circuit rejected the argument that the duplicate invoices were "counterfeited", and the Third Circuit subsequently rejected the argument that they were "forged as to the signature of" a person. Thus the two decisions relied upon by the petitioner were based upon mutually inconsistent interpretations of the bond.

The decision of the North Carolina Supreme Court in *Peoples Bank and Trust Company* v. *The Fidelity and Casualty Company*, *supra*, has no application to the facts of this case for the following reasons:

(1) The forgery in that case consisted of the signing of a name which purported to be and was presented as the signature of a person other than the signator. Here, there was no representation that Callahan's signature was that of any other person.

(2) The signature on a check is necessary to its validity. The signature of Callahan upon the duplicate invoices and the appearance thereon of the notations that he *had* assigned the account to the Bank was unnecessary, and was of no significance. They did not appear on the original invoices. Under North Carolina law, such an unnecessary signature could not constitute forgery.

(3) The copies of invoices signed or unsigned had no legal efficacy, or intrinsic value, and could not form the basis of any legal right, and under North Carolina law such papers could not be the subject of forgery.

Petitioner's argument with respect to forgery is completely answered by the Court of Appeals in the following language:

"Here, there is such a contention. It is founded upon the fact that all of the duplicate invoices deposited with the Bank bore a form of assignment and notice to the purported customer to remit to the Bank. Such notices of assignment had been affixed to all original invoices during the period when the notification procedure had been followed by the Bank and the Lumber Company. Such assignments and notices had been omitted from all original, valid invoices after the notification procedure was abandoned. For some reason, however, Callahan continued to affix such legends upon the duplicate invoices deposited with the Bank, and, in most instances, these were actually signed by J. W. Callahan for the lumber company.

"Falsity here did not reside in the assignment, however. The falsity lay in the implicit misrepresentation made to

the Bank when the Lumber Company deposited with the Bank the duplicate invoices. Certainly as the term "forgery" is commonly understood the fact that an instrument contains a false representation does not lead to the conclusion that the instrument is forged or "forged as to signature." The negotiator of a worthless check bearing his signature represents that he has on deposit sufficient funds with which the check may be paid, but, when he affixes his own signature to the worthless check and does not represent himself to be another, his crime is distinct from that of the forger. Moreover, here, the assignments and the execution of the assignments were quite unnecessary, for the deposit of the duplicate invoices under the loan agreement was quite sufficient, *inter sese*, for the transfer to the Bank of the rights of the Lumber Company in the receivable the duplicate invoice represented or purported to represent. In North Carolina, it has been held that falsification of a signature is not forgery, unless the signature is necessary to the validity of the instrument or the effectuation of the transaction." (citing *State* v. *Gherkin*, 29 N.C. 206, in which it was held that falsely putting a witness' name to a bond which was not required to be attested by a subscribing witness does not affect the validity of the bond and is therefore not a forgery.)

Not only was the signature of Callahan not necessary to effectuate the assignment of any account, neither the notation of assignment nor his signature served any purpose on the duplicate invoices. A similar notation had appeared upon the original invoices when customers had remitted direct to the Bank. The wording of the notation was not an assignment in itself, but merely a request to the customers. It was a relic of the notification practice, and was obsolete. Its continued use was surplusage, and

constituted no part of the invoice itself, did not mislead the Bank, and actually played no part in Callaham's fraudulent scheme. Under no circumstances could such a notation or signature thereto constitute forgery under the law of North Carolina.

Under North Carolina law, as pointed out by the Court in *Peoples Bank* v. *Casualty Company*, *supra*, there can be no "forgery" of a paper writing which if genuine would have no legal efficacy, and an invoice or unaccepted bill for goods has no legal efficacy or significance. As defined in that decision forgery is "the false making with intent to defraud of any writing, which, if genuine, might apparently be of legal efficacy or the foundation of a legal liability."

The North Carolina Court also held that the erasure or obliterating of a release on the back of a bond is not a forgery, despite the intent to defraud, *State* v. *Danbury*, 28 N.C. 70 (1845), and that the signing of the name of a candidate for Congress to a statement in an advertisement purporting to indicate the candidates views of proposed legislation does not constitute forgery, because the candidate could not be held liable for a breach of such expression of views or promises if his signature were genuine, *Barnes* v. *Crawford*, 115 N.C. 76 (1894).

The true nature of the fraud practiced upon petitioner by Callaham, and its exclusion from the bond is fully described by the Court of Appeals as follows:

"Of course, the Lumber Company and its officers Callaham were guilty of gross misrepresentation and of false pretense, but losses upon loans secured by such means are not within the coverage of the bond. The deposit of the duplicate invoice carried with it the implicit representation

that the customer whose name appeared thereon had ordered goods which the lumber company had delivered or shipped, that the purchase price was the amount which appeared upon the invoice that the purchase price had not been paid, and that the customer had no offsetting claims against the Lumber Company. These same representations were contained in more explicit form in the loan agreement, though the Bank, and apparently no one else, has suggested that the loan agreement, on that account, is counterfeited or forged as to signature. The financial statements which the Lumber Company filed with the Bank and upon which the Bank relied were equally false, for they included in reported accounts receivable all of these spurious transactions. The ledger sheets which reflected these fictitious transactions, which the Bank inspected and upon which the Bank relied, were similarly false, but no more can be said of any of these instruments, including the duplicate invoices, than that they were all part of the scheme of misrepresentation of the Lumber Company's sales and outstanding receivables. All of them were clearly the acts of Callaham and of the Lumber Company, and there was no misrepresentation of the person or persons responsible for them. The duplicate invoices, as the other writings used to effect and maintain the misrepresentation, cannot be said to have been "counterfeited or forged as to signature."

It is therefore apparent that the delivery of the duplicate invoices to the Bank was no more than another form of Callaham's many forms of representing that the assigned accounts receivable were genuine and outstanding.

The statutes of North Carolina use the expressions "forge" and "counterfeit" synonymously. Section 14-119 of the General Statutes of North Carolina provides punish-

ment for any person who "shall falsely make, forge or counterfeit . . . any bill, or note imitation of . . . a bill or note of a bank or of the State". Section 14-120 of these statutes punishes the uttering of such "forged" or "counterfeited" paper. General Statutes 14-122 provides punishment for any person who shall "falsely forge and make, . . . any deed, lease, or other notes, assignments, receipt for any security for the payment of money, or order for the money or goods, or release for any security for the payment of money, or order for the payment of money".

Again, these statutes refer to the false making of instruments which possess intrinsic value, have legal efficacy, or which can form the basis of a legal obligation or right, and which is represented to be the act of a person other than the person signing the same.

On the other hand, the statutes of some states define forgery broadly enough to include the act of "falsely making" any paper writing for the purpose of defrauding another person. As stated in *Provident Trust Co.* vs. *National Surety Company*, *supra*, cited by petitioner, "under the law of Pennsylvania the making of a false statement in a warehouse receipt is a forgery".

Our contentions regarding the law of forgery are supported by the following decisions which are cited in the opinion of the Court of Appeals:

*Greathouse* v. *United States*, 4 Cir., 170 F. 2d 512, 514

*United States* v. *Brotea*, 2 Cir. 246 F. 2d 541

*Martoccy* v. *United States*, 10 Cir. 216 F. 2d 709

*Goetcher* v. *The State of Nebraska*, 113 Neb. 352, 204 N.W. 967

*United States* v. *Mulligan*, 2 Cir., 59 F. 2d 200

The decision in the instant case is also in accord with the decision of this Court in *Gilbert v. United States*, 370 U.S. 650, 82 S. Ct. 1572 8 L. Ed. 801, to the effect that where the falsity of an instrument lies in the representation of facts contained in the instrument and not in the genuineness of its execution, it is not a counterfeit or a forgery. A similar result was reached by the Third Circuit in *United States v. Carabasi*, 292 F. 2d 362, decided since the Fidelity Trust case.

*The bond is not ambiguous, and under the well established rule of the North Carolina Court and of this Court its terms should be given their usual and ordinary meaning.*

As shown by the opinion of the Court of Appeals, and the other decisions above discussed, the provisions of the bond are not ambiguous. Therefore, petitioner can obtain no assistance from its contention that in the event of an ambiguity a contract should be construed against its author. As before stated, petitioner's statement of the question here presented incorrectly assumes the existence of an ambiguity. Petitioner's contention on this point is answered by the Court of Appeals as follows:

> "As in South Carolina, it is settled in North Carolina that insurance contracts are to be construed as other contracts, and that, in the absence of ambiguity, the terms are to be given their usual and ordinary meanings, the objective being to discover and enforce the real intention of the parties."

*Powers v. Travelers' Company*, 180 N.C. 335, 119 S.E. 481

*McCain* v. *Hartford Live Stock Ins. Co.*, 190 N.C. 549, 130 S.E. 186;

*Bailey* v. *Life Ins. Co. of Va.*, 222 N.C. 716, 24 S.E. 2d 614

*Ford* v. *New York Life Ins. Co.*, 222 N.C. 154, 22 S.E. 2d 235

*Bolich* v. *Provident Life & Accident Ins. Co.*, 205 N.C. 43, 169 S.E. 826

*McDaniel, Administratrix*, v. *Imperial Life Insurance Company*, 243 N.C. 275, 90 S.E. 2d 546

*Marshall* v. *Washington National Insurance Co.*, 246 N.C. 447, 98 S.E. 2d 345

This is in accord with the rule adhered to by this Court, and by all of the Courts of this country, and no further expression of this Court upon this subject is needed. *Bergholm* v. *Peoria Life Insurance Company*, 284 U.S. 480, 52 S. Ct. 230.

*Petitioner's Status as a National Bank is Immaterial.*

The fact that the petitioner is now a National Bank which status it acquired after its losses were incurred, does not raise any question under federal laws, nor does it constitute any reason for granting the petition.

This action involves a private contract between private parties. The Bankers Blanket Bond, Standard Form No. 24, herein involved, was said in the findings of fact in the Bank of Memphis case to have been worked out between the Surety Association of America and the American Bankers Association for use in all states. Its terms are

still subject to change. The interpretation of its terms are governed by the laws of the state in which it is issued.

As heretofore stated, the rule adhered to by this Court and the Supreme Court of North Carolina to the effect that the provisions of such a contract will be given their usual, natural and ordinary meaning, need no further pronouncement or clarification.

This reason for review was also urged in the petition for a Writ of Certiorari filed in *The First National Bank of Memphis* v. *Aetna Casualty and Surety Company*, *supra*.

## CONCLUSION

We submit that the law upon the questions here involved was well settled before the decision of the Court of Appeals in this case was rendered. Certainly any vestige of doubt as to the correctness of this law was dispelled by the clear and cogent reasoning of the Court of Appeals in its opinion herein; and a denial of the Petition would confirm this evaluation of the opinion.

There is no question herein presented which is of any public interest. While bonds similar to the one involved are issued throughout the country to various banks, both state and national, which are subject to such changes as might be worked out between the surety companies through their association and the banks through its association, no federal or constitutional question is involved. Since the interpretation of any such contract is determined by the laws of the state in which it is issued and made, a decision of this court would not necessarily be controlling

in other cases. Certainly, the petition fails to meet the requirement that any alleged conflict of opinion between the Courts of Appeal must be real and embarrassing before this Court will grant a petition for a Writ of Certiorari, and then only in cases involving a principle, the settlement of which is of importance to the public as distinguished from the parties to the litigation. *Rice* vs. *Sioux City Memorial Park Cemetery*, 349 U.S. 70, 75 S. Ct. 614, 99 L. Ed. 897.

It is, therefore, respectfully submitted that the Petition for a Writ of Certiorari should be denied.

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## APPENDIX

### EXCERPTS FROM PLAINTIFF'S EXHIBIT A—BOND (TR. 13)

* * *

The full text of Clause (E) is as follows:

"(E) Any loss through the Insured's having, in good faith and in the course of business, whether for its own account or for the account of others, in any representative, fiduciary, agency or other capacity, either gratuitously or otherwise, purchased or otherwise acquired, accepted or received, or sold or delivered, or given any value, extended any credit or assumed any liability, on the faith of, or otherwise acted upon any securities, documents or other written instruments which prove to have been counterfeited or forged as to the signature of any maker, drawer, issuer, endorser, assignor, lessee, transfer agent or registrar, acceptor, surety or guarantor or as to the signature of any person signing in any other capacity, or raised or otherwise altered or lost or stolen, or through the Insured's having, in good faith and in the course of business, guaranteed in writing or witnessed any signatures, whether for valuable consideration or not and whether or not such guaranteeing or witnessing is ultra vires the Insured, upon any transfers, assignments, bills of sale, powers of attorney, guarantees, endorsements or other documents, upon or in connection with any securities, obligations or other written instruments and which pass or purport to pass title to such securities, obligations or other written instrument; EXCLUDING HOWEVER, any loss through FORGERY OR ALTERATION of, or on any checks, drafts, acceptances,

withdrawal orders or receipts for the withdrawal orders or receipts for the withdrawal of funds of property, certificates of deposit, letters of credit, warrants, money orders or orders upon public treasuries; and excluding, further, any loss specified in subdivisions (1) and (2) of Insuring Clause (D) as printed in this bond, whether or not any amount of insurance is applicable under this bond to Insuring Clause (D).

Mechanically reproduced facsimile signatures are treated the same as handwritten signatures."

In addition to the exclusions of the bond quoted in the appendix to the plaintiff's brief in the Court of Appeals, the bond provided as follows:

EXCLUSIONS—Section 1. "THIS BOND DOES NOT COVER:

"(d) Any loss the result of the complete or partial nonpayment of or default upon any loan made by or obtained from the Insured, whether procured in good faith or through trick, artifice, fraud or false pretenses, except when covered by Insuring Clauses (A), (D) or (E)."